

**Before the Committee on Appropriations  
Subcommittee on Transportation, Treasury and  
Independent Agencies  
U. S. House of Representatives**

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# **Appropriations Issues for the Department of Transportation FY 2004 Budget**

**Statement of  
The Honorable Kenneth M. Mead  
Inspector General  
U.S. Department of Transportation**



Mr. Chairman and Members of the Subcommittee:

Thank you for inviting us to testify today as the Subcommittee begins its deliberations on the fiscal year (FY) 2004 appropriation for the Department of Transportation (DOT). At the outset, I want to express my appreciation for the support of Secretary Mineta, the DOT leadership, and the Congress for the work of the Office of Inspector General.

Over the past year, much of the focus at DOT has understandably been on security, and there are very notable achievements in this regard, particularly in the aviation arena. With the transfer of the United States Coast Guard and the Transportation Security Administration (TSA) to the newly created Department of Homeland Security (DHS), the coming year presents DOT with a renewed opportunity to focus on its core missions of transportation safety and mobility.

DOT must do this, however, in an extremely challenging budgeting environment. Revenues in the form of taxes and user fees are down sharply, and we have entered a period of deficit spending. The Congressional Budget Office recently estimated that the deficit will be \$246 billion in FY 2003, significantly higher than projections made just 3 months ago. At the same time, the Government is faced with new security costs, a potential war in Iraq, and growing demands for resources for existing programs including transportation.

The budget situation this year is especially difficult for DOT, since it relies so heavily on trust funds for financing. DOT trust fund revenues are down markedly. There are also increased program needs in all modes—from solving Amtrak's financial crisis to funding highway and aviation safety programs to funding construction that will increase aviation, highways, and transit capacity. This is occurring against the backdrop of the reauthorizations of three major DOT

programs, the Aviation Investment and Reform Act for the 21<sup>st</sup> Century (AIR-21), the Transportation Equity Act for the 21<sup>st</sup> Century (TEA-21), and Amtrak. Funding levels for these programs are obviously a policy call for Congress. In our opinion, there are opportunities to stretch existing Federal dollars by looking at key cost drivers in operations, acquisitions, and infrastructure investments to identify where costs can be contained or reduced, programs can be run more effectively and efficiently, and fraudulent activities can be detected and prevented.

Maintaining safety in all modes of transportation is an overarching challenge for all DOT Operating Administrations and a key strategic goal for the Department. The specific challenges in this area include reducing the over 40,000 fatalities and millions of injuries on our highways each year. Although motor carriers are only 4 percent of the vehicles on the road, they account for a disproportionate number of deaths each year. Commercial aviation is very safe, but in FY 2002, on average there was one serious runway incursion (that barely avoided or had significant potential for collision on the ground) every 10 days and one serious operational error (near collision in the air) every 8 days. The Federal Aviation Administration (FAA) has made progress in addressing this area, but it needs to continue to follow through on corrective action plans. In addition, FAA must remain vigilant in its oversight of air carriers to sustain the high level of safety during times when airlines are in financial distress. FAA has recognized the need and has taken steps to heighten safety surveillance of air carriers in distress. FAA also needs to pay close attention to the level of oversight it provides for repair stations—air carriers are turning to these facilities more and more as a way to reduce costs.

Much of the airline industry is in a precarious financial situation. With declines in revenue that are likely to persist, the major network carriers have found themselves with unsustainable cost structures. Self-help is the difficult but necessary solution in this restructuring effort. The Congress may find that the

financial condition of the airline industry results in additional requests for loan guarantees from the Airline Stabilization Board. Should the Board determine that an airline in financial straits has restructured its business, and its business plans are realistic, a loan guarantee that finances a carrier's exit from financial distress may be a prudent, short-term, market intervention that will likely provide long-term benefits to the public.

Ensuring air service to small communities is another potential cost driver that bears mentioning at this time. Small communities have a keen interest in the successful restructuring of the large network carriers. It is these carriers who connect small-hub and non-hub communities to the aviation system. In the last 3 years, from March 2000 to March 2003, non-hub airports lost 19 percent of their commercial air service as measured by scheduled passenger seats, and those in the Northeast and Midwest have lost approximately one-third of their service. Maintenance of service in these markets will be most successful where the restructuring of the network carriers is most successful. However, we know the funding levels for the Essential Air Service Program, which many small communities rely on to sustain limited air service, will be an important matter for the Committee's consideration this year.

Finally, DOT's central transportation safety and mobility missions clearly must interface with DHS's security responsibilities. This will require close interaction between the two Departments to strike an appropriate balance in implementing, regulating, funding, and overseeing programs that benefit the traveling public. A pending issue is the next phase of explosives detection system (EDS) deployment. Thus far, nearly all EDS equipment has been lobby-installed. TSA's planned next step (integrating the EDS equipment into airport baggage systems) is by far the most costly aspect of full implementation. We have seen estimates of those efforts at over \$3 billion. A key question is who will pay the cost of integrating EDS into

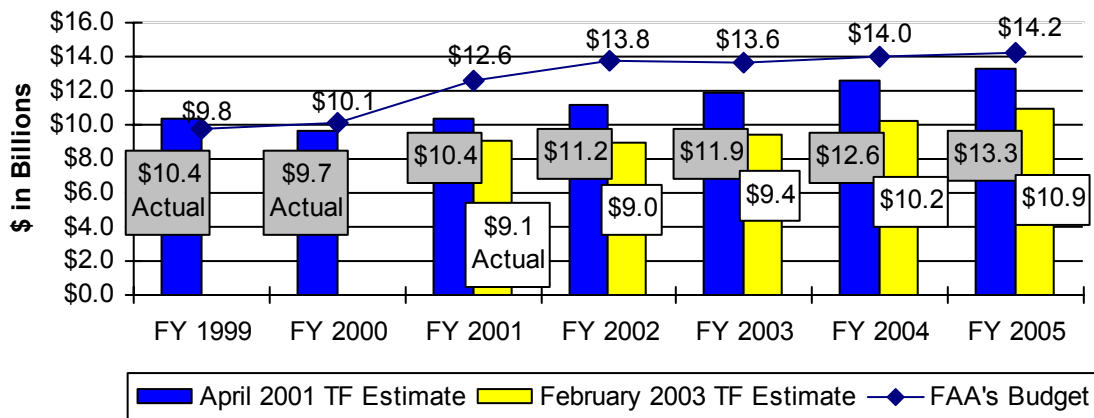
airport baggage systems at the Nation's largest airports, which will require structural changes at most airports.

***Funding DOT Programs in Light of Steep Declines in Trust Fund Revenues.***

DOT's total FY 2004 budget request is \$54.3 billion, of which \$46.2 billion (85 percent) is from DOT trust funds and \$8.1 billion (15 percent) is from the General Fund. Historically, the majority of DOT's budget has been covered by the Aviation and Highway Trust Funds. Revenue projections for both of these trust funds are down. The options for compensating for these declines are not attractive: raise taxes on users, limit investments in our congested transportation systems, shift the burden for these expenditures to state and local governments, and/or tap more of the General Fund just at the time when deficits have reappeared and the competition for these funds is rapidly increasing.

Aviation Trust Fund. Projected tax receipts to the Aviation Trust Fund for FY 2004 have dropped from approximately \$12.6 billion estimated in April 2001 to about \$10.2 billion estimated in February 2003. Over the next 4 years, Aviation Trust Fund tax revenues are expected to be about \$10 billion less than projections made in April 2001. Although Trust Fund projections are down for next year, FAA's spending request is not, increasing from \$13.6 billion this year to \$14.0 billion next year. If this \$3.8 billion gap between Trust Fund revenues and FAA's budget (\$10.2 billion to \$14.0 billion) is financed by the General Fund, it would represent a rough doubling of such spending compared to recent years.

### FAA: Decline in Estimated Trust Fund Revenues Compared to FAA's Budget

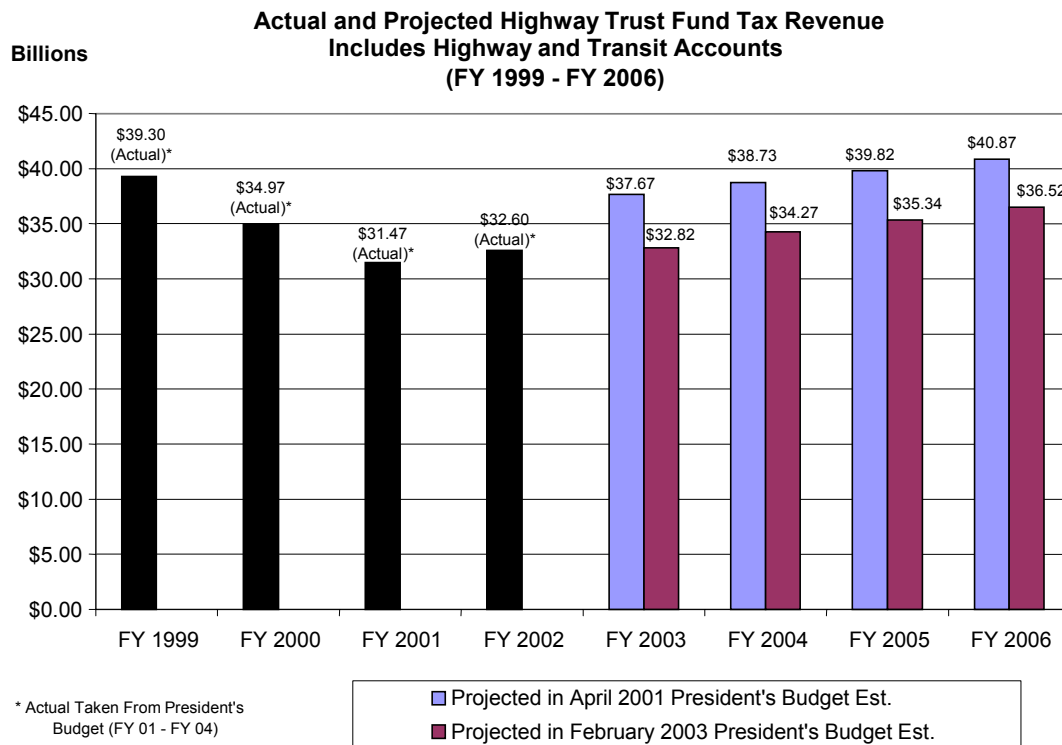


Although we have heard suggestions that this gap could be closed by increasing taxes or fees on airlines and air passengers, we urge extreme caution in this area. Taxes and fees are already high. Currently, nearly 26 percent of a \$100 non-stop airline ticket goes to taxes and fees. Any further increases are likely to reduce airline revenues, given the weak demand environment and will further threaten the financial health of the industry.

Highway Trust Fund. The fiscal health of the Highway Trust Fund is important to the Federal Highway Administration (FHWA), the Federal Motor Carrier Safety Administration (FMCSA), the Federal Transit Administration (FTA), and the National Highway Traffic Safety Administration (NHTSA) because they derive most or all of their funding from the Highway Trust Fund.<sup>1</sup> In recent years, tax receipts fell from \$39.3 billion in FY 1999 to \$31.5 billion in FY 2001, a 20 percent decline. Current estimates show that between FY 2003 and FY 2006, Highway Trust Fund tax revenues will be about \$18 billion less than projections made in April 2001. Tax receipts are not expected to return to the FY 1999 level until FY 2008. For FY 2004, the President's budget requests \$37.1 billion from

<sup>1</sup> These amounts are 100 percent for FHWA and FMCSA, 82.1 percent for FTA, and 81.0 percent for NHTSA.

the Highway Trust Fund, \$2.8 billion more than anticipated FY 2004 receipts of \$34.3 billion.



These decreased projections mean that highway and transit programs will see continuing constraints on their ability to improve mobility, safety, and economic growth unless taxes are raised, a greater portion of the financing burden is shared by state and local governments, or greater reliance is placed on the General Fund to supplement Trust Fund receipts. As with aviation taxes, the timing is not auspicious for a tax increase this year, since gas prices have risen to \$2 a gallon in some locations.

As for state and local governments, their revenues are down as well because of continuing weakness in economic growth and in the transportation sector in particular. Because these governments generally must balance their budgets on an

annual basis, they are already faced with potential tax increases and/or significant budget cuts in existing programs and are unlikely to be able to pick up a significantly increased share of the Nation's transportation costs.

As Congress and the Department move this year to reauthorize highway, aviation, and intercity passenger rail programs, tough decisions will have to be made by Congress as to what funding levels for individual programs are sustainable within this financial picture. When we look at DOT's budget, there are several actions that can be taken to operate more efficiently and effectively within this environment. These actions include reducing cost growth by controlling the cost drivers underlying that growth; leveraging Federal expenditures; and reducing fraud, waste, and abuse.

***Federal Aviation Administration.*** For FY 2004, FAA's budget request is \$14 billion, which is 26 percent of DOT's budget, representing a 3 percent increase above the FY 2003 appropriations of \$13.6 billion. FAA's budget request exceeds projected Aviation Trust Fund revenues in FY 2004 by over \$3 billion. Assuming no new taxes or fees, this shortfall will have to be made up either by drawing down the uncommitted balance of the Trust Fund or tapping the General Fund.

In 1996, Congress acted to make FAA a performance-based organization by giving the agency two powerful tools—personnel reform and acquisition reform. Congress also directed FAA to develop an effective cost accounting system. The expectation was that by relieving the agency from Government rules, FAA would operate more like a business. That is, services would be provided to users cost effectively, and air traffic control modernization programs would be delivered approximately on time and within budget.



Seven years later, we do not see sufficient progress toward achieving those outcomes. FAA's budget has grown from \$8.2 billion in FY 1996 to \$14 billion in FY 2004—an increase of \$5.8 billion, or over 70 percent. About 33 percent of this increase was a result of higher airport funding, and about 15 percent was a result of increases in FAA's modernization budget, but the largest portion of this increase (52 percent) was attributable to FAA's operating budget. During this period, we have also seen large cost overruns and schedule slips in FAA's major acquisitions. Continued growth of that magnitude is unsustainable, given the multibillion-dollar declines in projected Aviation Trust Fund receipts, and greater dependence of FAA on the General Fund.

- To date, the most visible results of personnel reform are increased workforce costs. While, there has been improved labor/management relations with controllers (FAA's largest workforce), FAA's operating costs, which are primarily payroll, have increased by \$3 billion, going from \$4.6 billion in FY 1996 to \$7.6 billion in FY 2004—an increase of over 65 percent. Much of that increase has been a result of salary increases negotiated under personnel reform. The new pay system for controllers was a significant cost driver. Between 1998 (when the new system was implemented) and 2003, the average base pay for controllers has increased 47 percent. This compares to an average salary increase for all other FAA employees during the same period of about 32 percent. Although linking pay and performance was a key tenet of personnel reform, only about 36 percent of FAA employees receive pay increases based on individual performance. The remainder of FAA employees receives largely automatic pay increases.

We also found that there are somewhere between 1,000 and 1,500 side bar agreements or Memorandums of Understanding (MOUs) that FAA managers entered into. Many serve legitimate purposes and are needed, but some MOUs

increase personnel costs significantly. However, FAA management does not know the exact number or nature of these agreements, there are no established procedures for approving MOUs, and their cost impact on the budget has not been analyzed. We briefed the FAA Administrator on our concerns regarding MOUs, and we are working with the Administrator and her staff to address this issue. The procedures for approving MOUs and understanding their fiscal impact are important matters to resolve as FAA deploys new technologies to field facilities.

- In terms of acquisition reform, results have been mixed—contracts are awarded more expeditiously, and FAA’s “build a little, test a little” approach has clearly avoided failures on the scale of the multibillion-dollar Advanced Automation System acquisition during the 1990’s. But the bottom line is that significant schedule slips for major air traffic control acquisitions and substantial cost growth are all too common. Five major acquisitions, largely managed since FAA was granted acquisition reform, have experienced cost growth of over \$3 billion (or the equivalent of one year’s budget for all modernization programs) and schedule slips of 3 to 5 years. Problems with cost growth, schedule slips, and performance shortfalls have serious consequences—they result in costly interim systems, a reduction in units procured, postponed benefits (in terms of safety and efficiency), or “crowding out” other projects.
- Congress directed FAA to have a fully functioning cost accounting system in 1996. However, over 6 years and \$38 million later, FAA still does not have a cost accounting system that covers the agency and provides managers with accurate cost data by location. Without such a cost accounting system, FAA cannot credibly claim to be, nor function as, a performance-based organization. To have an effective cost accounting system, FAA also needs an accurate labor

distribution system. Cru-X is the labor distribution system FAA chose to track hours worked by air traffic employees. As designed, Cru-X could have provided credible workforce data for addressing controller concerns about staffing shortages, related overtime expenditures, and to help determine how many controllers are needed and where. That information in turn is especially important given projections of pending controller retirements. Unfortunately, Cru-X as designed has not been implemented. We hope it will be in the coming year.

***Amtrak.*** Amtrak's FY 2004 budget request to the Congress totals \$1.812 billion.<sup>2</sup> The Administration, however, is requesting \$900 million: \$671 million for operating costs and \$229 million for maintenance and capital improvements. All of Amtrak's Federal funding traditionally has come from the General Fund.

In 1997, Congress passed the Amtrak Reform and Accountability Act requiring Amtrak to become operationally self-sufficient by 2003. Despite Amtrak's attempts to increase revenues and reduce costs, its losses are far greater now than in 1997 when the Act was passed. For FY 2002, Amtrak reported:

- \$1.3 billion in operating losses (up from \$797 million in FY 1997);
- \$681 million in cash losses (up from \$549 million in FY 1997);
- \$4.8 billion in debt and capital lease obligations (up from \$1.7 billion in FY 1997);
- \$250 million to \$300 million in annual debt service requirements (up from \$75 million in FY 1997); and

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<sup>2</sup> According to Section 24315(b)(1)(B) of Title 49 U.S.C., Amtrak "may include recommendations for legislation, including the amount of financial assistance needed for operations and capital improvements."

- continued growth in its capital investment backlog. Amtrak projects it will need to invest \$30 billion in capital projects over the next 25 years just to sustain the current system.

We are encouraged by improvements David Gunn has made since his appointment as President and Chief Executive Officer of Amtrak, such as management streamlining and workforce reductions in the hundreds and a willingness to provide more comprehensive operating and financial information to DOT and Congress. However, Amtrak's FY 2004 request contains two key assumptions that bear close scrutiny: Amtrak assumes productivity enhancements from work rule changes as a result of new labor agreements (although the successful negotiation of these agreements and any attendant savings are uncertain at this point). Second, Amtrak projects \$206 million in additional savings from actions as yet undefined.

We have heard claims that cutting long-distance routes would solve the current dilemma. This is a myth. Because of labor severance payments and other shutdown costs, it is unlikely there would be any short-term savings. It is also unlikely that the long-term savings from such a move would be large enough to eliminate the need for substantial financial support for the railroad's capital needs.

Lower-than-predicted revenues for the first 4 months of FY 2003 combined with more aggressive budget targets in the second half of the year means that Amtrak faces a significant challenge to avoid another cash crisis similar to the one experienced last summer. Moreover, as the debate on Amtrak's reauthorization and the future of inter-city passenger rail evolves, critical short-term and long-term funding decisions must be made.

***Federal Highway Administration.*** FHWA requested \$30.2 billion for FY 2004, all of which is from the Highway Trust Fund. FHWA represents 56 percent of DOT's budget.

Increased highway investment under TEA-21 has produced substantial benefits, but resource demands remain great. The number of active large highway projects has increased from 9 in 2000 to 17 today. Those 17 projects are estimated to cost more than \$41.3 billion, according to current FHWA estimates.

FHWA must ensure that major projects are delivered approximately on time, on budget, and free from fraud. Whether funds are lost to cost overruns, schedule delays, or fraud, the result is that fewer resources remain for transportation projects. To illustrate, if the efficiency with which the \$500 billion invested by the Federal Government and states over the last 6 years were improved by only 1 percent, an additional \$5 billion would be made available - enough to fund 4 of the 17 active large highway projects. (These projects are currently being monitored by FHWA's Office of Program Administration.)

We have seen several large projects that stand as examples of good project management practices—Utah's I-15 and the Alameda Corridor in California, for example. We have also seen ineffective management and oversight lead to significant cost increases, financing problems, schedule delays, and technical or construction difficulties on projects such as the Central Artery in Massachusetts, and the Springfield Interchange in Virginia.

Fraud is also a drain on financial resources. In the last few years, we have seen indictments for fraud triple, convictions double, and monetary recoveries of \$73 million. Our work does not suggest abuse on a scale such as was experienced in the 1950s and 1960s. Nonetheless, at present, we have 98 pending

investigations of contract and grant fraud in 35 states. The types of fraud we are commonly seeing today include false claims, product substitution, Davis-Bacon Act violations, bid-rigging, Disadvantaged Business Enterprise (DBE) fraud, and corruption of public officials. Secretary Mineta and the Department have been very supportive of our effort to aggressively prevent and detect fraud in this program.

Although FHWA has taken initial steps to improve its stewardship, much more needs to be done to ensure that Federal funds are used effectively and are protected from fraud, waste, and abuse. Actions FHWA should take include:

- Transitioning from reviewing contract-level actions to a higher-level oversight role focused on improving state management practices in areas such as preparing cost estimates, designing projects, monitoring schedules, and planning;
- Establishing minimum standards for cost estimates so that such basic cost items as inflation, construction management, design, and adequate contingency resources will not be excluded from estimates of what a highway program will cost;
- Ensuring that State Transportation Improvement Programs (3-year plans) are financially constrained and properly represent to the tax payers the highway and bridge projects a state will realistically undertake and finance;
- Ensuring that major projects use proven project management tools including finance plans that show how much a project will cost, its schedule and where the money is coming from;

- Modernizing its staffing structure to move from an engineering culture to a more multi-disciplined workforce with the management, financial, environmental, program analysis, and engineering oversight skills needed to review modern highway projects and programs;
- Establishing a debarment and suspension policy to ensure that people who defraud one DOT program cannot defraud another; and
- Supporting legislative changes to allow recoveries and civil penalties to be retained by states who suffer losses as a result of fraud.

***Federal Transit Administration.*** FTA's FY 2004 budget request totals \$7.22 billion, of which \$5.93 billion will come from the Highway Trust Fund and \$1.29 billion from the General Fund. The Department estimates that through 2020 an average annual capital investment of \$14.8 billion in Federal, state and local funds will be required to maintain the condition and performance of the Nation's transit assets at their 2000 level.

Given the demand for transit investments, there are several options for ensuring that project costs are contained and that communities are encouraged to explore cost-effective transit solutions.

- Continuing strong oversight of FTA grantees. FTA has institutionalized the use of project management oversight contractors (PMOCs) and financial management oversight contractors (FMOCs) to oversee transit projects and to report to its in-house staff on findings and needed corrective actions. This is essentially a sound approach that can provide early warnings of cost, schedule, financing and quality problems. Over the past 2 years, we have seen significant strengthening in FTA's oversight of its grantees. FTA and its

contractors must remain vigilant in ensuring that project costs are contained, schedules do not slip, and funds are available to complete the projects.

- Encouraging communities to be more cost-conscious when evaluating alternative transportation solutions before requesting Federal funding. For example, the Miami-Dade Transit Agency expanded its existing busway system, after determining that a heavy rail system would have cost 10 times as much to build, and a light rail system would have cost 4 times as much in comparison with a busway.

FTA has also suggested that reducing the cap on the Federal share of New Starts funding from 80 percent to 50 percent of project costs would allow them to fund more New Starts projects. However, we are uncertain regarding the likely impact of this proposal. First, the funding pattern since the enactment of TEA-21 shows that the Federal share of New Starts projects has averaged 45 percent. Second, while Federal New Starts money may be limited to 50 percent, it needs to be made clear whether grantees can use Federal transit formula and other Federal funds to increase the percentage of Federal funding to well above 50 percent.

***Maritime Administration.*** The Maritime Administration (MARAD) is a new budget account for this subcommittee. MARAD's FY 2004 budget request is \$219 million, which comes from the General Fund. The two major cost drivers at MARAD are:

- MARAD's Title XI Loan Guarantee Program, which assists private companies in obtaining financing for ship construction or shipyard modernization. After a period of stability, nine loans have defaulted in the last 5 years, totaling approximately \$490 million, and representing about 11 percent of MARAD's \$4.3 billion portfolio. To pay the \$330 million in loan guarantees due in



FY 2002, MARAD borrowed \$136 million from the Treasury and paid \$194 million from reserves financed by fees on guaranteed loans. To date, MARAD has repaid \$124 million to the Treasury. We are close to issuing a final report on this program that was requested by Senator McCain.

- MARAD's requested \$11.4 million in FY 2004 for its Ship Disposal Program, which is legislatively mandated to dispose of MARAD's obsolete vessels by FY 2006. These vessels comprise merchant and non-military ships in MARAD's National Defense Reserve Fleet that have deteriorated to a point where they are no longer operational. This request, along with the \$31.2 million appropriated in FY 2003, will provide for the dismantling of 14 to 18 of the 130 obsolete ships. Of the FY 2003 funds, \$20 million was provided by the Department of Defense (DOD). However, it is uncertain how much, if any, funding MARAD will receive from the DOD in FY 2004. Also, at the current average cost of \$2.5 million per ship, even continuance of the FY 2003 funding level would not enable MARAD to dispose of all its obsolete vessels by the deadline. MARAD's inventory of obsolete vessels has almost doubled in the last 6 years because MARAD's ships are becoming obsolete at a faster rate than MARAD can dispose of them. MARAD must find a faster and more cost-effective solution, as these ships are deteriorating, contain hazardous substances, and pose an immediate environmental threat, which will be difficult given the limited domestic ship disposal market.

This concludes our summary overview of the Department's FY 2004 budget request. The remainder of this testimony goes over the Operating Administrations in greater detail, providing our insights on the Department's budget request and the performance challenges facing these Operating Administrations.

## FEDERAL AVIATION ADMINISTRATION

In 1996, Congress acted to make FAA a performance-based organization by giving the agency two powerful tools: personnel reform and acquisition reform. Congress also directed FAA to develop an effective cost accounting system so that it would know, at the facility level, where it was spending money and for what. The expectation was that by relieving the agency from Government rules and establishing a cost accounting system, FAA would operate more like a business—that is, services would be provided to users cost effectively and air traffic control modernization programs would be delivered approximately on time and within budget.

Seven years later, we do not see sufficient progress toward achieving those outcomes. FAA's budget has grown from \$8.2 billion in FY 1996 to \$14 billion in FY 2004—an increase of \$5.8 billion, or over 70 percent. About 33 percent of this increase was a result of higher airport funding, and about 15 percent was a result of increases in FAA's modernization budget, but the largest portion of this increase (52 percent) was attributable to FAA's operating budget. During this period, we have also seen large cost overruns and schedule slips in FAA's major acquisitions. Continued growth of that magnitude is unsustainable. Given the fiscal situation and multibillion-dollar declines in projected Aviation Trust Fund receipts, FAA must become performance-based in deeds as well as words.

***Controlling Operating Cost Increases.*** To date, the most visible results of personnel reform are increased workforce costs. During this period, there has been improved labor/management relations with controllers (FAA's largest workforce). However, FAA's operations budget, which is 82 percent payroll costs, has increased from \$4.6 billion in FY 1996 to \$7.6 billion in FY 2004 – an increase of over 65 percent. Much of the increase has been a result of salary increases negotiated under personnel reform. The 1998 collective bargaining agreement with the National Air Traffic Controllers Association (NATCA), which created a new pay system for FAA's controllers, was a significant cost driver. Under the agreement, most controllers' salaries increased substantially. For example,

- The *average* base salary for fully certified controllers has now risen to over \$106,000 – a 47 percent increase over the 1998 average of about \$72,000. This compares to an average salary increase for all other FAA employees during the same period of about 32 percent, and for all Government employees in the Washington, D.C. area of about 30 percent.

Although linking pay and performance was a key tenet of personnel reform, only about 36 percent of FAA employees receive pay increases based on individual

performance. The remainder of FAA employees receive largely automatic pay increases

We also found that there are between 1,000 and 1,500 side bar agreements or MOUs that FAA managers have entered into with NATCA. Many serve legitimate purposes and are valid, but a number of MOUs we reviewed were not cost-effective and, in our opinion, not in the best interest of the Government. For example,

- One MOU we reviewed allows controllers transferring to larger consolidated facilities to begin earning the higher salaries associated with their new positions substantially in advance of their transfer or taking on new duties. At one location, controllers received their full salary increases 1 year before their transfer (in some cases going from an annual salary of around \$54,000 to over \$99,000). During that time, they remained in their old location, controlling the same air space, and performing the same duties.

Although some MOUs can have significant financial implications, FAA management does not know the exact number or nature of these agreements, there are no established procedures for approving MOUs, and their cost impact on the budget has not been analyzed. We briefed the FAA Administrator on our concerns regarding MOUs, and we are working with the Administrator and her staff to address this issue.

***Improving Acquisition Management.*** Acquisition reform results have been mixed—contracts are awarded more expeditiously, and FAA’s “build a little, test a little” approach has clearly avoided failures on the scale of the multibillion-dollar Advanced Automation System acquisition. But the bottom line is that significant schedule slips and substantial cost growth for major air traffic control acquisitions are all too common. The following chart provides cost and schedule information on five projects largely managed since FAA was granted acquisition reform.

| Program                                              | Estimated Program Costs<br>(Dollars in Millions) |             | Percent Cost Growth | Implementation Schedule |                          |
|------------------------------------------------------|--------------------------------------------------|-------------|---------------------|-------------------------|--------------------------|
|                                                      | Original                                         | Current     |                     | Original                | Current                  |
| Wide Area Augmentation System                        | \$892.4                                          | \$2,922.4*  | 227 %               | 1998-2001               | 2003-To Be Determined**  |
| Standard Terminal Automation Replacement System      | \$940.2                                          | \$1,690.2** | 80 %                | 1998-2005               | 2002- To Be Determined** |
| Airport Surveillance Radar-11                        | \$752.9                                          | \$916.2     | 22 %                | 2000-2005               | 2003-2008                |
| Weather and Radar Processor                          | \$126.4                                          | \$152.7     | 21 %                | 1999-2000               | 2002-2003                |
| Operational and Supportability Implementation System | \$174.7                                          | \$251.0     | 44 %                | 1998-2001               | 2002-2005                |

\* This includes the cost to acquire geostationary satellites and costs are under review.

\*\*Costs and schedules are under review by FAA.

These five acquisitions have experienced cost growth of over \$3 billion and schedule slips of 3 to 5 years. Problems with cost growth, schedule slips, and performance shortfalls have serious consequences - they result in costly interim systems, a reduction in units procured, postponed benefits (in terms of safety and efficiency), or “crowding out” other projects. For example:

- In FY 2002 alone, FAA reprogrammed over \$40 million from other modernization efforts (data link communications, oceanic modernization, and instrument landing systems) to pay for cost increases in the Standard Terminal Automation Replacement System.

There are large-scale acquisitions - both old and new - whose cost or schedule baselines need to be revised because the programs have changed considerably or benefits have shifted. For example, the Integrated Terminal Weather System (ITWS) provides air traffic managers with enhanced weather information. FAA planned to complete deployment of the new weather system in 2004 at a cost of \$286 million. However, unit production costs have skyrocketed from \$360,000 to over \$1 million; FAA cannot execute the program as scheduled and may extend the deployment by 4 years.

In addition, the Local Area Augmentation System (LAAS) is a new precision approach and landing system. FAA intended to have LAAS (Category I, which provides basic services) operational in 2004. This date cannot be met because of

additional development work, evolving requirements, and unresolved issues regarding how the systems will be certified as safe for pilots to use. Moreover, the more demanding Category II/III service planned for 2005 is now a research and development effort with an uncertain end date.

***Implementing Cost Controls.*** To effectively manage its costs and genuinely operate like a business, FAA needs an accurate cost accounting system with an effective labor distribution system, and needs to follow sound business practices in administering its contracts.

- The 1996 Reauthorization Act for FAA required the agency to develop a cost accounting system in order to track agency costs and provide managers with needed cost data by location. However, after over 6 years and \$38 million, FAA is now planning to complete its cost accounting system by September 2003, assuming no further slippage. Without a reliable cost accounting system, FAA cannot credibly claim to be, nor function as, a performance-based organization.
- To have an effective cost accounting system, FAA also needs an accurate labor distribution system. Cru-X is the labor distribution system FAA chose to track hours worked by air traffic employees. As designed, Cru-X could have provided credible workforce data for addressing controller concerns about staffing shortages, related overtime expenditures, and to help determine how many controllers are needed and where. That information in turn is especially important given projections of pending controller retirements. Unfortunately, Cru-X as designed has not been implemented. We hope it will be in the coming year.
- We have consistently found a lack of basic contract administration at every stage of contract management from contract award to contract closeout. For example, we found that Government cost estimates were: prepared by FAA engineers, then ignored; prepared using unreliable resource and cost data; or, worst of all, prepared by the contractor (a conflict of interest). FAA is in the process of following through on its commitments to address this issue.

***Other Significant Issues That Will Require Attention.*** There are three other issues that need to be considered in the upcoming appropriations.

- A major issue for airports is funding the next phase of EDS integration. Thus far, nearly all EDS equipment has been lobby-installed. TSA's planned next step (integrating the EDS equipment into airport baggage systems) is by far the most costly aspect of full implementation. We have seen estimates that put the

costs of those efforts at over \$3 billion. A key question is who will pay for those costs and how.

While the current Airport Improvement Program (AIP) has provided some funding in the past for aviation security, we urge caution in tapping this program until we have a firm handle on airport safety and capacity requirements. In FY 2002, airports used over \$561 million of AIP funds for security-related projects. In contrast only about \$56 million in AIP funds were used for security in FY 2001. Continuing to use a significant portion of AIP funds on security projects will have an impact on airports' abilities to fund capacity projects.

- FAA's Operational Evolution Plan (OEP) for enhancing airport capacity needs to be updated in light of September 11<sup>th</sup> and the financial condition of the airlines. FAA is working to retool the OEP. FAA needs to synchronize the OEP with FAA's budget, set priorities, and address uncertainties with respect to how quickly airspace users will equip with new technologies. It also needs to ensure that the costs associated with multibillion-dollar modernization projects not in the OEP are considered when establishing priorities and are integrated with OEP initiatives. It is a good time to rethink what reasonably can be accomplished over the next 3 to 5 years.
- In the current financially-strapped aviation environment, FAA must remain vigilant in its oversight to sustain a high level of aviation safety. FAA has recognized this need and has taken steps to heighten surveillance during times when airlines are in financial distress. For example, FAA has increased the number of inspections planned for distressed air carriers' internal aircraft maintenance operations. FAA also needs to pay close attention to the level of oversight it provides for repair stations. In the past 5 years, there has been a significant increase in air carriers' use of these facilities. In 1996, major air carriers spent \$1.6 billion for outsourced maintenance (37 percent of total maintenance costs), whereas in 2001, the major air carriers outsourced \$2.9 billion (47 percent of total maintenance costs). This trend is likely to continue, and FAA needs to consider the shift in maintenance practices when planning its safety surveillance work.

## FINANCIAL HEALTH OF THE AIRLINE INDUSTRY

Much of the airline industry is in a precarious financial situation. With what are likely to be permanent changes in the nature of business demand,<sup>3</sup> the major network carriers have found themselves with unsustainable cost structures that must be revamped on two fronts: labor costs and the cost and productivity of capital. Self-help is the difficult but necessary solution in this restructuring effort.

An exception may be the loan guarantees provided by the Air Transportation Stabilization Board. In addition to their generally weak financial condition, airlines are beset by uncertainty, more so than most industries, from the prospects of war or further acts of terrorism. In this environment, access to the private financial markets is difficult or nonexistent for the large network carriers. Loan guarantees, if prudently incurred, can help to stabilize the financial condition of the industry and not simply be used to avoid making hard choices.

The Congress may find that the financial condition of the airline industry results in additional requests from the Board. Should the Board determine that an airline in financial straits has restructured its business and its business plans are realistic, a loan guarantee that helps to finance their exit from financial distress may be a prudent, short-term market intervention that will likely provide long-term benefits to the public, particularly if taxpayers are adequately compensated for the risks the Government will incur. We believe the Board has done a reasonably good job in achieving this goal.

Small communities have a keen interest in the successful restructuring of the large network carriers. It is these carriers, in both their mainline operations and those of their regional affiliates, who connect small-hub and non-hub communities to the aviation system. Maintenance of service in these markets will be most successful where restructuring of the cost structures of the network carriers is most successful.

This is all the more important given the long-term trend at non-hub airports (airports that individually handle less than 0.05 percent of enplaned passengers nationwide). For the last 5 years, these airports have seen a continuous decline in their service. At the same time, service to larger airports was growing until the downturn in business travel 2 years ago. Just in the last 3 years, from March 2000 to March 2003, these airports lost 19 percent of their commercial air service as measured in scheduled passenger seats, and some parts of the Nation have seen

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<sup>3</sup> Business travelers have constituted 20 percent of air travelers, but provided about 50 percent of the revenue, according to some airlines. It is unlikely that business travelers in the future will be willing to sustain the high fares necessary to generate this level of revenue.

even greater cuts, with non-hub airports in the Northeast and Midwest losing approximately one-third of scheduled air service.

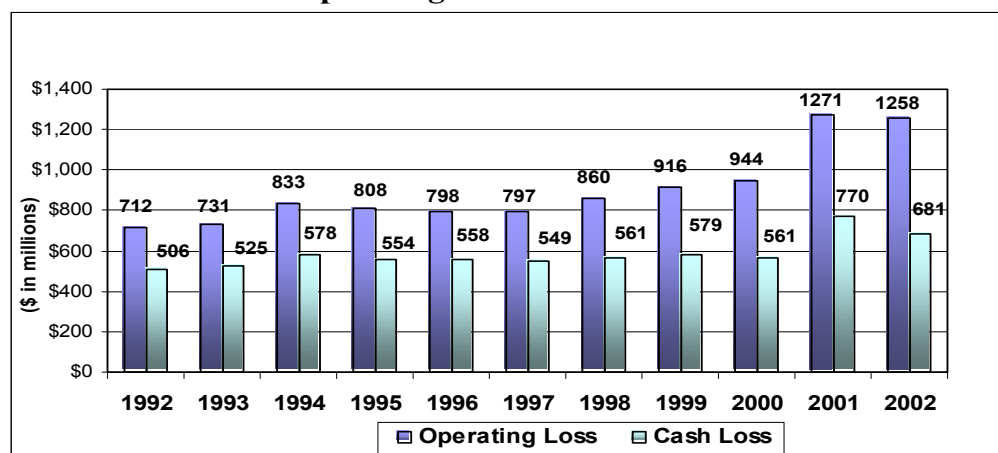
Many small communities rely on the Essential Air Service (EAS) program as a means of sustaining limited air service, funding this program will continue to be a challenge given the anticipated growth in the number of communities seeking assistance and the significantly increased average subsidy levels, which rose from \$79 to \$229 per passenger (190 percent) between 1995 and 2002. The President's FY 2004 budget proposes significant changes to EAS, including lowering funding to \$50 million from over \$100 million in FY 2003 and restricting the eligibility of communities for subsidies. We know the funding level for this program will be an important matter for the Committee's consideration this year.

## AMTRAK

Amtrak depends on Federal, state, and local subsidies to supplement its revenue earned from operating passenger rail service across the Nation. For FY 2004, the Administration requested \$900 million for Amtrak, but Amtrak asked for \$1.812 billion.

Despite Amtrak's attempts to increase revenues and reduce costs to become operationally self sufficient, its losses are far greater now than in 1997, when Congress passed the Amtrak Reform and Accountability Act. Amtrak's annual Federal funding over the last 5 years has averaged about \$1.1 billion. Even with that funding, Amtrak has not been able to meet its operating and capital requirements.

**Amtrak Operating and Cash Loss: 1992 - 2002**

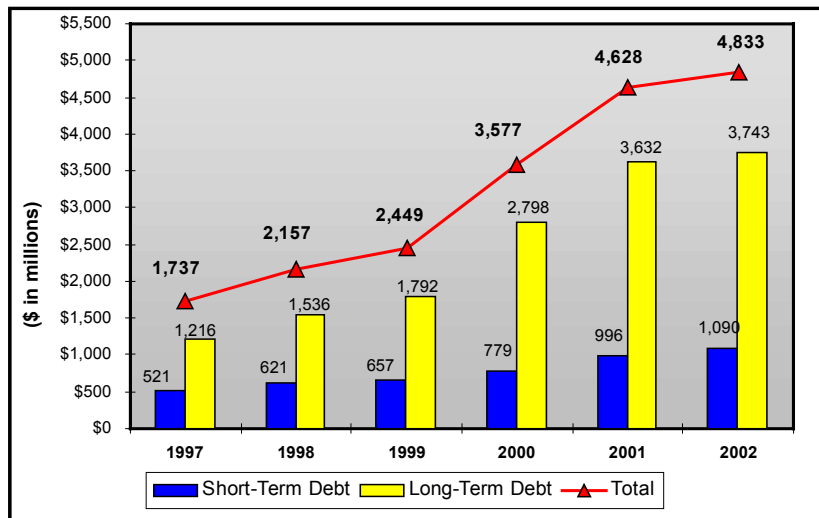




### *A Look at Amtrak's Track Record for FY 2002 Paints a Stark Picture*

- Amtrak earned about \$2.3 billion in revenue - over 40 percent of which came from non-passenger sources such as transporting mail and access fees for use of its rail infrastructure. However, operating expenses topped \$3.5 billion.
- Amtrak reported an operating loss of \$1.3 billion, a cash loss of \$681 million, and short- and long-term debt and capital lease obligations of \$4.8 billion (up from \$1.7 billion in 1997). This has saddled Amtrak with annual debt service requirements ranging from \$250 million to \$300 million (up from \$75 million in 1997).

#### **Amtrak Debt: 1997 - 2002**



NOTE: Amtrak's Consolidated Balance Sheet also lists Deferred Credits and Other Liabilities such as casualty and environmental reserves, as well as post-retirement employee benefits obligations, totaling an additional \$1.2 billion.

- Amtrak's deferred capital investment backlog continued to grow; estimates for the Northeast Corridor alone are \$5 billion to \$6 billion. Amtrak projects it will need \$30 billion in capital investments over the next 25 years just to sustain the current system.
- To make ends meet in 2002, Amtrak required an emergency supplemental appropriation of \$205 million and a \$100 million direct loan from DOT. In total, Amtrak received approximately \$1.2 billion in Federal funds for FY 2002.

***Improvements Seen Under New Leadership Encouraging, but Cannot Solve Amtrak's Problems on Their Own.*** On a positive note, since Mr. Gunn assumed leadership at Amtrak last spring, we have seen management streamlining and workforce reductions of hundreds of positions and a willingness to provide more comprehensive operating and financial information to DOT and Congress. However, Amtrak's problems cannot be solved simply by finding savings within the current structure. The problem is too big and too fundamental to the system. We have heard claims that cutting long-distance routes would solve the current dilemma. This is a myth. Because of labor severance payments and other shutdown costs, it is unlikely there would be any short-term savings. It is also unlikely that the long-term savings from such a move would be large enough to eliminate the need for substantial financial support for the railroads' capital needs.

***FY 2003 - Another Difficult Year for Amtrak.*** Congress appropriated \$1.05 billion for Amtrak in FY 2003 and deferred payment of the \$100 million direct loan from FY 2002. Therefore, the appropriation was equivalent to an appropriation of \$1.15 billion. This is \$50 million less than Amtrak's request of \$1.2 billion. The appropriation establishes requirements for Amtrak to provide reports to the Secretary of Transportation and Congress on its operating and capital plans, its actions to implement new cost sharing procedures with states served with short-distance trains, and measures to reduce the financial burden on the Federal treasury of long-distance trains. The Secretary of Transportation was directed to assume a more rigorous oversight role by reviewing Amtrak's requests for grant funds and certifying the accuracy of financial information Amtrak provides to Congress.

Mr. Chairman, we see FY 2003 as another difficult year for Amtrak. Through January 2003, its cash losses were \$73 million larger than for the same period last year, and Amtrak's budget for the second half of the year presents more aggressive revenue and expense targets. In our view, Amtrak faces a significant challenge to avoid another cash crisis similar to the one experienced last summer.

***Facing the Future of Inter-City Passenger Rail.*** Considering Amtrak's recently submitted grant request of \$1.812 billion for FY 2004 (more than double the Administration's request of \$900 million), we would like to offer the following four points:

- There is no inter-city passenger rail trust fund, so Amtrak's Federal appropriation has traditionally come from the General Fund.
- The Administration's grant request includes only \$229 million for maintenance and capital improvements. This amount is substantially short of what Amtrak needs to cover its debt service requirements and to maintain the railroad

infrastructure and equipment in reasonably good working order. The difference must come from somewhere.

- Even at the \$1.8 billion level, Amtrak's request does not include the repayment of the \$100 million direct loan to the Department and safety and security needs identified in proposals following September 11, 2001.
- Amtrak's request contains two key assumptions that bear close scrutiny:
  - Amtrak assumes productivity enhancements from work rule changes as a result of new labor agreements. The successful negotiation of these agreements and any attendant savings are uncertain at this point.
  - Amtrak projects \$206 million in additional savings from actions as yet undefined.

Amtrak's 5-year authorization expired September 30, 2002. Critical short-term as well as long-term funding decisions will need to be made as the debate on Amtrak's future, and the future of inter-city passenger rail, evolves.

## **FEDERAL HIGHWAY ADMINISTRATION**

The FY 2004 Budget Request includes \$30.2 billion for FHWA, all from the Highway Trust Fund. The request creates a \$1 billion program to fund "ready to go" highway projects aimed at alleviating traffic bottlenecks and improving infrastructure conditions. The budget also focuses on improving transportation safety, which remains the Department's top priority.

***Increased Highway Investment Has Produced Substantial Benefits, but Resource Demands Remain Great.*** The combined Federal, state, and local investment in highways during the 6-year period of the Transportation Equity Act for the 21<sup>st</sup> Century (TEA-21) will exceed \$500 billion – an average expenditure of more than \$225 million a day. These investments have produced substantial benefits. According to FHWA, the percentage of highway mileage with an "acceptable" ride quality rose from 82.5 percent in 1993 to 86.0 percent in 2000. The percentage of bridge deck area considered deficient dropped from 30.9 percent in 1996 to 27.9 percent in 2000. However, despite the historic investment in highway infrastructure, the traveling public still faces significant congestion and delays on a daily basis.

Continuing to maintain and enhance our highway infrastructure will require large investments. As of March 2003, there are 17 active large highway projects estimated to cost \$41.3 billion. Another 25 planned projects are expected to cost \$43 billion, and 21 active and planned large corridor projects will cost \$42 billion.

**Top Highway Mega-Projects by Dollar Value  
Active Projects**

| <b>Project Name</b>                                                      | <b>Project Cost<br/>(Billions)</b> |
|--------------------------------------------------------------------------|------------------------------------|
| Central Artery/Ted Williams Tunnel – Boston, MA                          | \$14.6                             |
| Interstate 64/Hampton Roads Third Crossing – Hampton, VA                 | 4.4                                |
| Central Texas Turnpike – Austin, TX                                      | 3.6                                |
| Interstate 95/Woodrow Wilson Bridge – DC, MD, VA                         | 2.6                                |
| Interstate 80/San Francisco/Oakland Bay Bridge (East Span) – Oakland, CA | 2.6                                |
| Southeast Corridor (Highway Portion – Interstates 25/225) – Denver, CO   | 1.7                                |
| Interstate 10/Katy Freeway – Houston, TX                                 | 1.6                                |
| New Mississippi River Bridge – St. Louis, MO/IL                          | 1.4                                |
| New Ohio River Bridges (Kentucky/Indiana) – Louisville, KY               | 1.4                                |
| Miami Intermodal Center – Miami, FL                                      | 1.3                                |
| State Road 210/Foothill Freeway – Los Angeles, CA                        | 1.1                                |
| Marquette Interchange, Interstates 94/43/794 – Milwaukee, WI             | 1.1                                |
| Interstate 95/New Haven Harbor Crossing – New Haven, CT                  | 1.0                                |
| Interstates 4/275 – Tampa, FL                                            | 1.0                                |
| Springfield Interchange Interstates 95/395/495 – Springfield, VA         | 0.7                                |
| Cooper River Bridges – Charleston, SC                                    | 0.7                                |
| State Road 125 South Toll Road – San Diego, CA                           | 0.5                                |
| Total:                                                                   | \$41.3                             |

***Effective Stewardship of These Investments Is Essential - Especially When Resources Are Limited.*** Congress, the Administration, and state governments are all stakeholders in ensuring the investments in large projects result in a high quality transportation system. These are complex and challenging projects that should be delivered to the taxpayer approximately on time, on budget, and free from fraud and other irregularities. As Secretary Mineta has said several times, “My credo on waste, fraud, and abuse is simple: If a project calls for concrete and it’s a ten sack job, we at DOT are going to be sure we don’t end up with a seven sack job.”

We have seen several large projects that stand as examples of good project management practices - Utah’s I-15 and the Alameda Corridor in California are examples. On the other hand, we have seen ineffective management and oversight lead to significant cost increases, financing problems, schedule delays, and technical or construction difficulties. These projects include the Central Artery in Massachusetts and the Springfield Interchange in Virginia. Costs for the Springfield Interchange Project increased over 180 percent from \$241 million to \$677 million. In part, the cost increases occurred because State officials excluded known or easily identifiable costs, including basic items such as construction management, inflation, preliminary engineering, and even design. In addition, the baseline estimate was prepared far too early and was based on plans that were only 15 to 20 percent complete. Virginia was able to exclude these costs because FHWA had not established minimum standards for states to follow when

preparing cost estimates, nor had FHWA really scrubbed the estimates Virginia provided.

Whether funds are lost to cost overruns, schedule slippage, or fraud, the result is that fewer resources remain for transportation projects. Therefore, improving project management can provide significant benefits. To illustrate, if the efficiency with which the \$500 billion invested over the last 6 years were improved by only 1 percent, an additional \$5 billion would be made available - enough to fund 4 of the 17 active large highway projects.

We believe the states and FHWA have learned important lessons from problem projects, and are committed to improving management and oversight of large projects. The Federal Highway Administrator has strongly emphasized the importance of improving FHWA's oversight and accountability over funds, and the FY 2004 budget request recognizes that FHWA needs to improve its oversight activities for major projects.

Based on our audit work, which includes reviews of 18 major projects, we see continued opportunities for improved management, oversight, and increased vigilance. Overall, we see several opportunities to improve project delivery.

***Refocusing FHWA Oversight to Ensure That Major Projects Are Delivered Approximately On Time and On Budget.*** FHWA has historically focused most heavily on oversight of engineering and contract issues, rather than on oversight of management and financial processes. For example, FHWA still performs many detailed contract administration actions, such as approving contract change orders and the location and wording of highway signs.

Because FHWA remains focused on detailed engineering activities, rather than developing a more multi-disciplinary staff and higher-level approach to oversight, it has sometimes missed larger management issues. For example, at the time the Central Artery announced a \$1.4 billion cost increase in 2000, FHWA had approved thousands of design changes. Nonetheless, they were caught unaware when a cost increase was announced, even though they had just approved the project's finance plan.

Although FHWA has taken several steps to improve its stewardship, it needs to transition from its traditional role of reviewing and approving contract-level actions, to a new higher-level role of conducting reviews to ensure the effectiveness of the states' processes in areas that are major project drivers, such as financing, project-level cost estimates, schedule performance, transportation planning, and accountability over funds.

In reviewing large projects, we have identified a number of tools that can help managers keep projects approximately on time and on budget. These tools include reliable cost estimates, project finance plans, achievable state transportation program plans, and integrated master schedules. Finally, information is critical for policy makers as they decide which projects would be the best use of resources to address transportation problems and promote economic development. However, we found several troubled highway projects in which these tools were not used, or were not used effectively. For example, several large projects were not using the full capability of their schedule tools, and thus, did not have the information needed to deal with the inevitable schedule conflicts that arise in complex projects employing multiple contractors.

FHWA has a skills imbalance because its workforce is structured almost exclusively around engineering skills that were needed more during construction of the interstate system. Of FHWA's workforce of 2,860 employees, 1,130, or approximately 40 percent, are highway engineers. Today's highway projects require skills in emerging technologies and professional expertise in financing, cost-estimating, program analysis, and schedule management, yet FHWA has limited staff devoted to these areas. Engineering skills will remain important, but FHWA also needs a workforce with the skills and competencies needed for oversight and stewardship. This is not, however, to suggest that FHWA needs more staff. A strategy for achieving a more multi-disciplinary approach to oversight activities could include a mix of actions such as:

- hiring staff with private sector project management skills, such as financing and cost estimating; and
- adopting the Federal Transit Administration's practice of using contractors to oversee project and financial management.

An FHWA task force has been working since April 2000 "to evaluate the current and future needs of the FHWA workforce," and it plans to develop and deploy a Human Capital Plan in FY 2003.

***Promoting Efforts to Prevent, Detect, and Prosecute Fraud in the Federal Aid Highway Programs.*** Congress, the Federal Government, and state governments are all concerned with preventing fraud and abuse in transportation projects. In the past 3½ years, the Office of Inspector General has seen significant increases in our fraud case work and in judicial actions involving highway and transit projects. We have seen indictments for fraud triple, convictions double, and monetary recoveries of \$73 million during this period.

At present, we have 98 pending investigations of contract and grant fraud in 35 states. The types of fraud we are commonly seeing today include false claims, product substitution, Davis-Bacon Act violations, bid-rigging, Disadvantaged Business Enterprise (DBE) fraud, and corruption of public officials. For example, the case load includes 22 DBE investigations, an increase of 14 percent from the end of last fiscal year.

Under the law, FHWA can debar contractors convicted of fraud from doing further business with the Government. FHWA can also suspend contractors from participating in new Federal contracts if they are under indictment for fraud. However, there is no Department-wide policy on suspensions and debarments, and FHWA is sometimes reluctant to impose these sanctions.

States normally do not receive a portion of fines and monies recovered in successful fraud prosecutions. Fines and recoveries from such judgments are returned to the Federal Treasury. Since the states' programs are damaged by the fraud that leads to the enforcement action, sharing in the recoveries would help them restore their programs and provide support for further fraud deterrence efforts.

An example of this occurred in a civil settlement with Contech Construction Products, Inc., and Ispat-Inland, Inc., which involved product substitution in Louisiana. The companies substituted sub-standard polymer-coated steel culvert pipe used in highway and road construction projects from 1992 through 1997. Under the settlement agreement, the United States and Louisiana shared in a \$30 million recovery. Louisiana received \$5.2 million to compensate for the cost of the investigation and losses due to the product substitution.

Key actions DOT can take in its continuing fight against fraud include: (1) establishing a Department-wide debarment and suspension policy; (2) providing specialized fraud prevention training at the Federal and state level; and (3) supporting legislative changes to allow recoveries and civil penalties to be retained by the states.

## **FEDERAL TRANSIT ADMINISTRATION**

The Federal Transit Administration's (FTA) FY 2004 budget request totals \$7.22 billion, of which \$5.93 billion will be from the Highway Trust Fund and \$1.29 billion from the General Fund. As shown in Table 1, the FY 2004 request proposes distributing most of these funds as formula grants—a significant change in the program from FY 2003.

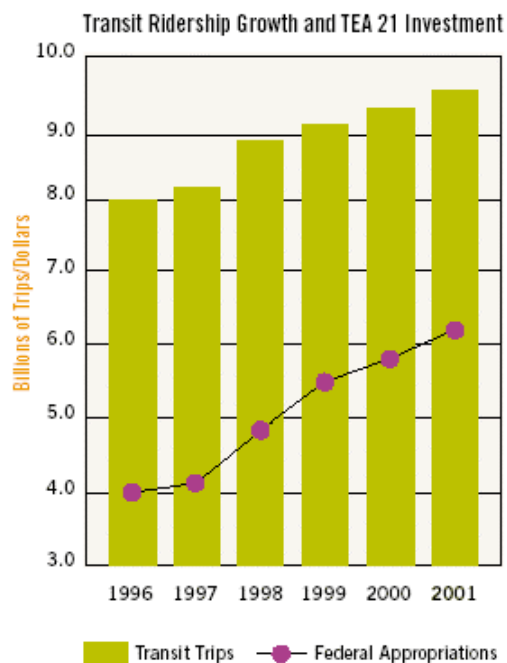
| Table 1. FTA Budget Categories         |                 |                 |
|----------------------------------------|-----------------|-----------------|
|                                        | 2003<br>Actual  | 2004<br>Request |
| <b>Formula Grants and Research</b>     |                 | \$5,615,000,000 |
| <b>Formula Grants</b>                  | \$3,839,000,000 |                 |
| <b>Major Capital Investment Grants</b> |                 |                 |
| <b>Capital Investment Grants</b>       |                 |                 |
| <b>New Starts</b>                      | \$1,214,400,000 | \$1,515,000,000 |
| <b>Modernization</b>                   | \$1,214,400,000 |                 |
| <b>Bus</b>                             | \$607,200,000   | \$19,000,000    |
| <b>Job Access and Reverse Commute</b>  | \$150,000,000   |                 |
| <b>Research and Planning</b>           | \$122,000,000   |                 |
| <b>Other</b>                           | \$79,000,000    | \$77,000,000    |
| <b>TOTAL</b>                           | \$7,226,000,000 | \$7,226,000,000 |

FTA's budget proposal also reflects sustained Federal funding at record high levels, which over the last 6 years, has contributed to a ridership increase of 1.76 billion (or 22 percent). The Department estimates that an average annual capital investment of \$14.8 billion would be needed just to maintain the current transit system through FY 2020.

The chart (below) shows FTA's annual appropriations compared to transit trips.

Given the demand for transit investments, there are several options for ensuring that project costs are contained and that communities are encouraged to explore cost-effective transit solutions that would stretch the Federal funding benefits:

***Continuing Strong Oversight of FTA Grantees.*** FTA's oversight program has come a long way since it was initially authorized in 1987 to oversee the implementation of major capital projects. FTA has institutionalized the use of project management oversight contractors (PMOCs) and financial





management oversight contractors (FMOCs) to oversee transit projects and to report to its in-house staff on findings and needed corrective actions. This is essentially a sound approach that can provide early warnings of cost, schedule, financing and quality problems. Nonetheless, the quality of PMOC/FMOC oversight can be improved, particularly in the areas of spot-checking grantee cost and schedule estimates. In our May 2000 review of the Tren Urbano project we determined that while the PMOC had raised important schedule and construction quality issues, it accepted the transit agency's cost representations without checking them. Similarly, our April 2001 review of the Seattle Central Link Light Rail project disclosed that FTA, through its contractors, had not performed due diligence in reviewing the project's cost and schedule. After sharing our findings with FTA, it took corrective action. Overall, the attention FTA is placing on strengthening the PMOC/FMOC process is positive, and sustaining these improvements will be important.

***Encouraging Communities to be More Cost-Conscious when Evaluating Alternative Transportation Solutions Before Requesting Federal Funding.*** With the demand for transit funds, a greater emphasis on lower cost options may help expand the benefits of Federal funding for mass transit. FTA can help expand awareness of alternatives, such as bus rapid transit, to building light or heavy rail systems that in the right circumstances can be more cost-effective. For example, bus rapid transit systems cost an average of \$680,000 to \$13.5 million per mile and light rail systems average \$12.4 million to \$118.8 million per mile could leverage the Federal dollar. Some communities have already implemented lower cost options, such as the Miami-Dade Transit Agency. The agency expanded its existing busway system, after determining that a heavy rail system would have cost 10 times as much to build, and a light rail system would have cost 4 times as much in comparison with a busway.

FTA has also suggested that reducing the cap on the Federal share of New Starts funding from 80 percent to 50 percent of projects costs would allow them to fund more New Starts projects. Under TEA-21, the New Starts program continues to be the Federal Government's primary financial support for locally planned and operated transit guideway investments. Currently, there are over 150 projects in FTA's New Starts pipeline that are estimated to cost \$42 billion, for which project sponsors are seeking \$20 billion of Federal funds. FTA's FY 2004 budget submission requests \$1.5 billion. To be able to meet not only current commitments, but to also fund the most meritorious projects in the New Starts pipeline, FTA's proposal would limit the Federal share of New Starts funding to 50 percent of project costs.

While this proposal would, in theory, allow more projects to receive funding, local planners have indicated it would discourage investment in transit projects.

However, a 50 percent New Starts cap would, in part, reflect a funding pattern that has emerged in the program since 1991. During this period the Federal investment in New Starts projects averaged 45 percent, even though TEA-21 authorized up to an 80 percent Federal share. However, we are uncertain about the likely impact of this proposal. While New Starts money may be limited to 50 percent, it needs to be made clear where grantees can use Federal transit formula and other Federal funds to increase the percentage of Federal funding to well above 50 percent.

## **MARITIME ADMINISTRATION**

The Maritime Administration (MARAD) is a new budget account for this subcommittee. MARAD's FY 2004 budget request is \$219 million, which would be covered by the General Fund. We find that there are two major cost items in MARAD's budget.

***Title XI Loan Guarantee Program.*** MARAD's Title XI Loan Guarantee Program assists private companies in obtaining financing for ship construction or shipyard modernization. Currently the program consists of approximately \$4.3 billion in loan guarantees and commitments. Applicants have requested an additional \$5.8 billion. MARAD's budget request for FY 2004 is approximately \$4 million for administration costs. No funds were requested for new loan guarantees.

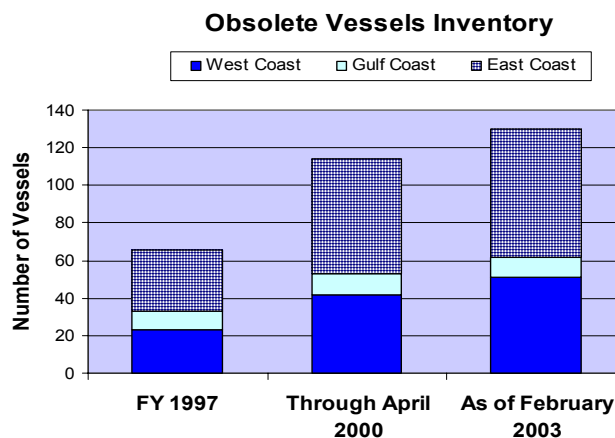
- After a period of stability, nine loans have defaulted in the last 5 years, totaling approximately \$490 million, representing about 11 percent of MARAD's \$4.3 billion portfolio. Defaults make MARAD responsible for assuming loan payments and entitle MARAD to recoup part of these costs through the sale of the defaulter's assets. As of January 2003, of the \$490 million paid out by MARAD due to defaults, it recouped 18 percent of the funds.
- In FY 2002, MARAD borrowed \$136 million from the Treasury in order to pay almost \$330 million in loan guarantees due to loan defaults. (The other \$194 million came from MARAD's reserves financed by fees on guaranteed loans.) To date, MARAD has repaid \$124 million to the Treasury. The balance of \$12 million is due by 2005.

Because of these loan defaults, we were requested by Senator McCain to review MARAD's Title XI Loan Guarantee Program. We are close to issuing a final report. Based on MARAD's comments to our draft report, the agency is cognizant of the need for improved administration and oversight of the program.

***Ship Disposal.*** MARAD is legislatively mandated to dispose of all of the 130 obsolete vessels in its inventory by FY 2006. These vessels comprise merchant and non-military ships in MARAD's National Defense Reserve Fleet

that have deteriorated to a point where they are no longer operational. It has requested \$11.4 million in its FY 2004 budget request for the Ship Disposal Program. This request, along with the \$31.2 million appropriated in FY 2003 for ship disposal, will provide for the dismantling of approximately 14 to 18 of the 130 obsolete ships in its National Defense Reserve Fleet. Of the amount appropriated in FY 2003, \$20 million was provided by the Department of Defense (DOD). As a result, MARAD's progress relies heavily on the level of funding provided by DOD. However, it is uncertain how much, if any funding; MARAD will receive for ship disposal from the DOD in FY 2004.

Even if funding were maintained at FY 2003 levels, it would not be sufficient for the disposal of all of the vessels in MARAD's inventory by the legislatively mandated deadline. MARAD's inventory of obsolete vessels grows by an average of 11.7 vessels per year, and as shown below, has almost doubled in the last 6 years.



At an average cost of \$2.5 million per ship, MARAD needs to find a more cost-effective solution for disposing of its obsolete vessels. However, the limited domestic ship disposal market and environmentally hazardous materials involved make ship disposal a costly undertaking. Further, many of the vessels are costly to keep afloat and are threatening environmental damage as they deteriorate in place.

## **FEDERAL MOTOR CARRIER SAFETY ADMINISTRATION**

The Federal Motor Carrier Safety Administration's (FMCSA) FY 2004 budget request of \$447 million, all from the Highway Trust Fund, is a 22 percent increase over FY 2003. The Department continues to make safety a top priority. By far, the greatest number of transportation-related fatalities involve motor vehicles.

Highway crashes claim at least 40,000 lives annually, of which more than 5,000 involve motor carriers, i.e. large trucks and passenger buses.

The key points we would like to make today concerning cost drivers in FMCSA's budget request are:

***Using Border Enforcement Staff Effectively.*** FMCSA's FY 2004 budget request includes \$66 million for border inspections and operations. Congress established requirements in its FY 2002 Appropriations Act to ensure that some very basic safeguards would be in place when the U.S.-Mexican border opens to long-haul commercial traffic, which included directing the Office of Inspector General to verify that FMCSA met the Act's requirements.

In June 2002, we reported that FMCSA had made substantial progress and had actions in process and planned to meet the Act's safety requirements. Safety requirements were to hire and train enforcement personnel, and establish inspection facilities and safety procedures at the southern border. We are performing a follow-up audit as required by the Act to verify that FMCSA completed the actions in process and planned. We expect to issue the report shortly.

On November 20, 2002, the Secretary certified that authorizing Mexican carrier operations throughout the United States does not pose an unacceptable safety risk. However, allowing Mexican carriers to operate throughout the United States has been delayed. This delay is the result of a ruling by the United States Court of Appeals for the Ninth Circuit citing the Department's failure to conduct in-depth environmental analyses. We, at present, do not know how long the delay will be.

Currently, border inspectors perform safety inspections of Mexican commercial vehicles and drivers operating in the commercial zones along the U.S.-Mexico border. Until the delay is resolved, safety auditors and safety investigators hired and trained to perform safety audits and compliance reviews of Mexican long-haul carriers are available to assist with other safety priority programs such as the new entrant program for U.S. and Canadian carriers.

***Using Certified Private Contractors to Perform Safety Audits for New Entrant Motor Carriers.*** Historically, FMCSA receives 40,000 to 50,000 new motor carrier applications annually. In May 2002, FMCSA established new, stricter minimum requirements to improve the safety performance of new U.S. and Canadian motor carriers by ensuring they are knowledgeable about applicable Federal motor carrier safety standards. These new entrant rules were effective in January 2003 and require a safety audit within the first 18 months of operation in order to receive permanent Department of Transportation registration.

FMCSA requested \$33 million in its FY 2004 budget for the new entrant program and proposes to use \$16 million for Federal resources and \$17 million to expand States' Motor Carrier Safety Assistance Program grants. The Motor Carrier Safety Improvement Act of 1999 authorizes the use of properly certified private contractors to perform safety audits, which could be a cost saving measure. FMCSA should explore this option as well, with an emphasis on strong Federal oversight.

***Improving the Credibility and Integrity of the Commercial Driver's License Program.*** FMCSA's FY 2004 request includes a \$10.8 million increase for the Commercial Driver's License (CDL) Program, bringing the total CDL Program budget to \$22 million. Our audits and investigations identified the need to strengthen the oversight of the CDL program and clarify Federal standards for issuing CDLs.

The subcommittee should consider linking this funding increase to a FMCSA requirement that States use covert procedures<sup>4</sup> to monitor driver examiners. In May 2002, we reported that the magnitude of fraud in the CDL program warranted the required use of covert procedures, and FMCSA's response to our report indicated an endorsement, and not a requirement, to use covert procedures.

In our May 2002 report, we stated existing Federal standards and State controls were not sufficient to defend against the alarming threat posed by individuals who seek to fraudulently obtain CDLs. For example, we found that only 4 of 13 States we visited had laws requiring applicants to demonstrate that they are citizens or legally present in the United States. Since 1998, we have conducted over 70 criminal investigations in 12 States involving CDLs. As of January 2003, these cases have resulted in 81 indictments, 63 convictions, and over \$480,000 in fines, restitution and other monetary recoveries. As a result, truckers have had their licenses suspended or revoked, or have had to be retested in order to ensure that they were qualified to drive commercial vehicles. Since 1998, Federal and State investigations have identified at least 13,000 commercial drivers that needed to be retested.

***Ensuring the Quality of Safety Performance Data.*** FMCSA is a data-driven agency and its success in reducing fatalities and injuries depends on the quality of its safety performance data. In FY 2004, FMCSA requested an information management program budget of \$38 million to maintain and improve its information systems.

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<sup>4</sup> Covert procedures are when the examiner does not know he or she is being monitored.

FMCSA uses a Safety Status Measurement System (SafeStat) to identify high-risk carriers and target these carriers for compliance reviews. SafeStat scores and rankings along with safety performance data are posted on an internet web site by individual carrier. Industry has raised concerns about the validity of the SafeStat model to identify high-risk carriers and the quality of the safety performance data used.

We are currently reviewing SafeStat to determine: (1) does the model work, (2) how good is the data, and (3) how good are the systems for preventing or correcting bad data. We expect to complete this audit in April 2003.

## **NATIONAL HIGHWAY TRAFFIC SAFETY ADMINISTRATION**

The FY 2004 Budget Request includes \$665 million for the National Highway Traffic Safety Administration (NHTSA). Of this amount, \$126 million, or 19 percent, comes from the General Fund and \$539 million, or 81 percent comes from the Highway Trust Fund. This request reflects a transfer of \$222 million in existing safety belt and alcohol grant programs from FHWA to NHTSA and an increase of \$18 million for operations and research. Two important issues NHTSA is focusing on are:

- ***Following Through on TREAD Act Commitments.*** The request includes \$9.35 million for Defects Investigations, including development of a database to analyze trends in defect reports from vehicle and equipment manufacturers. Successful deployment of this system is key to giving NHTSA the ability to identify dangerous defects early. This system, estimated to cost \$6 million, is currently scheduled for completion in June 2003, a 3-month slip from the initial schedule. Manufacturers must begin reporting defect data for entry into this new system by August 31, 2003.
- ***Increasing Safety Belt Use.*** NHTSA estimates that raising seat belt use to 85 percent from the present 75 percent would save 4,600 lives annually. However, without an increase in the number of states that have primary safety belt laws,<sup>5</sup> we see no credible basis to forecast increases in seat belt use in excess of the recent trend of 1 percentage point per year. The budget request devotes \$100 million to primary safety belt performance grants. Those grants would be available only to states that have either adopted primary laws or achieved usage rates that meet or exceed those achieved by states with primary laws.

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<sup>5</sup> Primary safety belt laws permit law enforcement officers to stop drivers and issue citations solely for not using safety belts.

## FUNDING TRANSPORTATION SECURITY

DOT's responsibility for transportation safety and efficiency will inevitably overlap with the Department of Homeland Security's (DHS) responsibilities for transportation security, requiring close interaction between the two Departments to strike an appropriate balance in implementing, regulating, funding, and overseeing programs that benefit the traveling public.

One issue that needs to be addressed is whether - to what extent - DOT funds should be used to assist security initiatives.

- As noted in the earlier discussion on FAA, the greatest part of security upgrade costs lies ahead (estimated at \$3 billion) and some have already suggested DOT's Airport Improvement Program as a source to fund these costs. However, these funds are also needed for airport safety and capacity requirements.
- Other examples of this pressure on DOT funds for security purposes will likely occur in the future. For instance, if DHS issues regulations requiring specific security measures within all transit systems - will the transit systems be expected to absorb the costs, will the costs be eligible items for DOT transit grants, or will DHS have its own grant system to cover these costs?

The questions arising from these examples demonstrate the importance of deliberately working through these funding issues before requirements are set, and the importance of this Subcommittee, DOT, and the transportation industry being active in all development phases of DHS regulations affecting transportation.

**Computer Security.** A set of security challenges that clearly remains with DOT, and which is in great need of improvement, is computer security. DOT, has the 3<sup>rd</sup> largest IT investment among civilian agencies (with a \$2.7 billion FY 2004 request) and relies on computers for critical, high-visibility functions such as controlling air traffic. However, less than one-quarter of DOT's mission-critical systems have been certified as adequately secured. DOT must fix this material weakness and improve the failing IT security grade it received from Congress.

**Financial Statements and DOT Accounting System.** Finally, DOT must be able to provide this Subcommittee with accurate financial and cost information from state-of-the-art financial management and cost accounting systems. This year, the Department attained a clean opinion on its financial statements. However, the unqualified, or "clean" opinion, did not come without extraordinary effort by DOT and the auditors. DOT is implementing new systems that should provide DOT with reliable financial data. In 1997, DOT began to replace its obsolete

accounting system. However four of DOT's largest agencies, which account for about 80 percent of DOT's budget, have not yet transitioned to the new system, called Delphi. The current timetable calls for these four agencies to transition to Delphi between March and October 2003 - but the schedule has slipped several times already.

Mr. Chairman, that concludes my testimony. I would be pleased to take any questions.



The following pages contain textual versions of the graphs and charts found in this document. These pages were not in the original document but have been added here to assist screenreaders.

## FAA: Decline in Estimated Trust Fund Revenues Compared to FAA's Budget

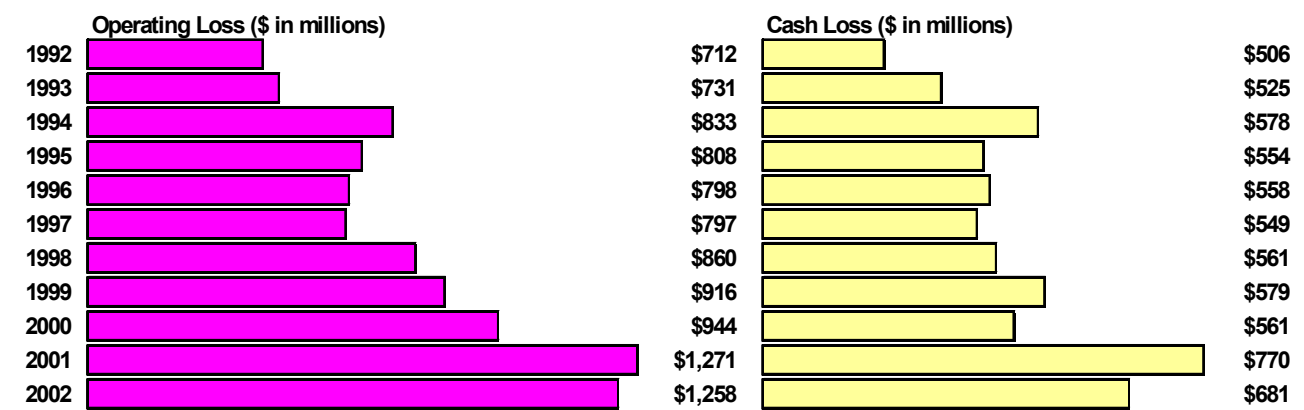
Pg 5 – FAA Table

| <u>Year</u> | <u>FAA's Budget</u> | <u>April 2001 Trust<br/>Fund Estimate</u> | <u>February 2003<br/>Trust Fund<br/>Estimate</u> |
|-------------|---------------------|-------------------------------------------|--------------------------------------------------|
| FY 1999     | \$9.8 Billion       | \$10.4 Billion<br>(Actual<br>Collection)  | Intentionally Left<br>Blank                      |
| FY 2000     | \$10.1 Billion      | \$9.7 Billion<br>(Actual<br>Collection)   | Intentionally Left<br>Blank                      |
| FY 2001     | \$12.6 billion      | \$10.4 Billion                            | \$9.1 Billion<br>(Actual<br>Collection)          |
| FY 2002     | \$13.8 Billion      | \$11.2 Billion                            | \$9.0 Billion                                    |
| FY 2003     | \$13.6 Billion      | \$11.9 Billion                            | \$9.4 Billion                                    |
| FY 2004     | \$14.0 Billion      | \$12.6 Billion                            | \$10.2 Billion                                   |
| FY 2005     | \$14.2 Billion      | \$13.3 Billion                            | \$10.9 Billion                                   |

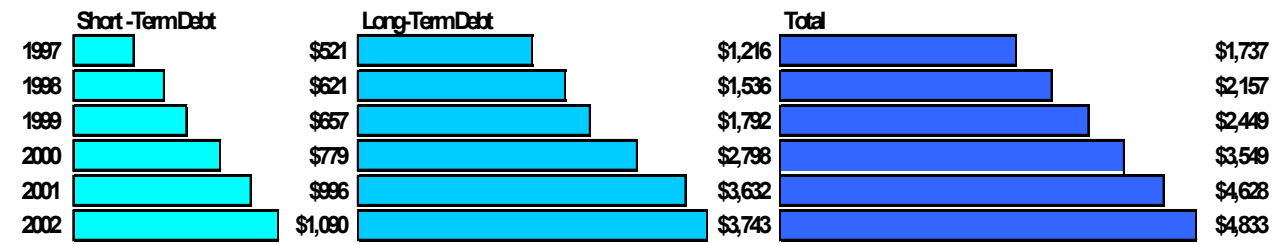
| <b>Projected Highway Trust Fund Tax Revenue</b><br><b>Includes Highway and Transit Accounts</b><br><b>(FY 1999 - FY 2006)</b> |                 |                                               |                                                  |
|-------------------------------------------------------------------------------------------------------------------------------|-----------------|-----------------------------------------------|--------------------------------------------------|
| <b>Trust Fund Tax Revenue</b>                                                                                                 | <b>Actual</b>   | <b>April 2001 President's Budget Estimate</b> | <b>February 2003 President's Budget Estimate</b> |
| <b>FY 1999</b>                                                                                                                | \$39.30 billion | N/A                                           | N/A                                              |
| <b>FY 2000</b>                                                                                                                | \$34.97 billion | N/A                                           | N/A                                              |
| <b>FY 2001</b>                                                                                                                | \$31.47 billion | N/A                                           | N/A                                              |
| <b>FY 2002</b>                                                                                                                | \$32.60 billion | N/A                                           | N/A                                              |
| <b>FY 2003</b>                                                                                                                | N/A             | \$37.67 billion                               | \$32.82 billion                                  |
| <b>FY 2004</b>                                                                                                                | N/A             | \$38.73 billion                               | \$34.27 billion                                  |
| <b>FY 2005</b>                                                                                                                | N/A             | \$39.82 billion                               | \$35.34 billion                                  |
| <b>FY 2006</b>                                                                                                                | N/A             | \$40.87 billion                               | \$36.52 billion                                  |

Pg. 6 – FHWA Table

### Amtrak Operating and Cash Loss: 1992 – 2002



## Amtrak Debt: 1997 - 2002



| <b>Transit Ridership Growth and TEA-21 Investment</b><br>(Billions of Trips/Billions of Dollars) |                           |                      |                           |                      |                           |
|--------------------------------------------------------------------------------------------------|---------------------------|----------------------|---------------------------|----------------------|---------------------------|
| <b>1996</b>                                                                                      |                           | <b>1997</b>          |                           | <b>1998</b>          |                           |
| Transit<br>Ridership                                                                             | Federal<br>Appropriations | Transit<br>Ridership | Federal<br>Appropriations | Transit<br>Ridership | Federal<br>Appropriations |
| 7.9                                                                                              | \$3.9                     | 8.3                  | \$4.2                     | 8.7                  | \$4.6                     |

| <b>Transit Ridership Growth and TEA-21 Investment</b><br>(Billions of Trips/Billions of Dollars) |                           |                      |                           |                      |                           |
|--------------------------------------------------------------------------------------------------|---------------------------|----------------------|---------------------------|----------------------|---------------------------|
| <b>1999</b>                                                                                      |                           | <b>2000</b>          |                           | <b>2001</b>          |                           |
| Transit<br>Ridership                                                                             | Federal<br>Appropriations | Transit<br>Ridership | Federal<br>Appropriations | Transit<br>Ridership | Federal<br>Appropriations |
| 9.1                                                                                              | \$5.3                     | 9.3                  | \$5.8                     | 9.5                  | \$6.3                     |

Source: American Public Transportation Association

| <b>Obsolete Vessel Inventory</b> |         |                    |                     |
|----------------------------------|---------|--------------------|---------------------|
| <b>Number of Vessels</b>         |         |                    |                     |
| Location                         | FY 1997 | Through April 2000 | As of February 2003 |
| West Coast                       | 23      | 42                 | 51                  |
| Gulf Coast                       | 10      | 11                 | 11                  |
| East Coast                       | 33      | 61                 | 68                  |